UNITED STATES BANKRUPTCY COURT

DISTRICT OF DELAWARE

In re:	:	Chapter 11
W.R. GRACE & CO., et al.,	:	Case No. 01-01139 (KG)
Reorganized Debtors.	:	

United States Bankruptcy Court

824 North Market Street

Wilmington, Delaware

September 19, 2017

11:01 a.m. - 12:17 p.m.

B E F O R E :

HON KEVIN GROSS

U.S. BANKRUPTCY JUDGE

ECRO OPERATOR: UNKNOWN

HEARING re Motion For Entry of an Order Enforcing Plan and Confirmation Order Against Internal Revenue Service [Filed: 4/12/17] (Docket No. 32854).

Transcribed by: Sonya Ledanski Hyde

A P P E A R A N C E S :

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P R O C E E D I N G S

CLERK: Please rise.

THE COURT: Good morning, everyone. You may be seated. Thank you. We're here, of course, in the W.R. Grace matter in a matter involving the Internal Revenue Service.

MR. O'NEILL: Yes, Your Honor. Good morning.

THE COURT: Good morning, Mr. Higgins -- not Mr. Higgins, I'm sorry -- Mr. O'Neill.

MR. O'NEILL: That's all right. You got that on the right side at least.

THE COURT: Yes.

MR. O'NEILL: That's good.

THE COURT: And I thank you all for understanding my problem yesterday with being here and allowing this to reschedule.

MR. O'NEILL: Your Honor, we don't view that as a problem.

THE COURT: All right.

MR. O'NEILL: And congratulations.

THE COURT: Thank you.

MR. O'NEILL: We're very happy to hear your news and glad everybody is happy and healthy.

THE COURT: Yes. Thank you, sir.

MR. O'NEILL: James O'Neill appearing on behalf of

the reorganized debtors from Pachulski Stang Ziehl & Jones. With me at counsel table is my co-counsel in this matter, Roger Higgins.

THE COURT: Yes.

MR. O'NEILL: And, Your Honor, the Court knows our client, Richard Finke, who is with us in the Courtroom today.

THE COURT: Mr. Finke, good morning.

MR. O'NEILL: General counsel of Grace. Your Honor, I'm going to turn the podium over to Mr. Higgins who's going to present our argument. Mr. Benson is here for the Department of Justice today.

THE COURT: All right. Is it not Mr. Benson who should go first, or does that not matter, Mr. Benson?

MR. BENSON: I'm happy to and, in fact, would like to. It is their motion.

MR. O'NEILL: It's our motion.

THE COURT: It's your motion, okay. All right.

MR. O'NEILL: So shall we?

THE COURT: Yes.

MR. O'NEILL: We'll start out?

THE COURT: Yes, you start out.

MR. O'NEILL: Okay, thank you.

THE COURT: I just wasn't sure burden of proof-wise who has the burden of proof on this claim issue. But I

guess it's really a legal argument at this point.

MR. O'NEILL: It is a legal argument, Your Honor.

THE COURT: Yeah. Yes, thank you. Mr. Higgins, good to see you again.

MR. HIGGINS: Well, thank you, Your Honor. Roger Higgins for the reorganized debtors. In fact, that -- you really sort of stole the first line, which really is, this is a legal argument.

THE COURT: Yes.

MR. HIGGINS: You know, unless counsel sees differently. I don't think there are any undisputed facts here, although I think it may take a couple of minutes to sort of get one's head around them. But when looked at, they're relatively simple and straightforward.

This all arises out of the tax year 1998, and a 10 or 11 year, I think it was, examination by the IRS that did not conclude until of 2009. A claim that was first -- a claim that was first filed in 2002 for $311 million by the IRS; subsequently amended to 11 million and some odd hundreds of thousands of dollars in 2012. The reorganized debtors came out of bankruptcy, went effective in February of 2014, and there were four IRS claims left among many others.

THE COURT: Yes.

MR. HIGGINS: Three of which were paid at 4.19

percent. They were allowed; there was no controversy over them. And the 11 million and change claim was objected to by the reorganized debtors in April of 2014.

At issue there was the tax amount, the -- and the allow -- what should be the allowed amount of the claim be. And one of the components of that proof of claim, that claim, was the post-petition interest, which the IRS had claimed at the statutory rate. In the -- ultimately, the claim was resolved between the IRS and the reorganized debtors, settlement -- settled in compromise. And the form of that settlement and compromise came through in the form of a withdrawal of the objection by the reorganized debtors and a withdrawal of the claim by the IRS.

Suffice it to say, there was no settlement agreement, quite frankly because the IRS didn't want to enter into a settlement agreement, and so we did this rather convoluted settlement and compromise. And that settlement and compromise gave the reorganized debtors the ability to allow claims or have them disallowed or compromise them pursuant to Section 5.1 of the plan without having the need for a final order.

So in April of 2014, and, indeed in September of 2014 when the IRS finally sent its refund to Grace, the decision was taken by Grace to essentially call a stop to this claim, agree to the tax amount from 1998, which was

$5.5 million, a little over 5.5 million -- $5.8 million -- excuse me -- and a certain amount of prepetition interest, which led to a total of about $6.72 million as of the petition date.

THE COURT: Yes.

MR. HIGGINS: So there was clearly a claim existing at the time of the objection and of the -- and of this settlement and compromise.

What the IRS has argued -- and the issue today here is not what interest was paid after March 15th of '09 when the claim was, the sort of the as-of date, the notional date on which the claim was satisfied, not the amount of interest that the IRS was paying on the refund amount post-3/15/09. But instead, the sole issue is what's the post-petition interest amount to be paid on that claim from April 2nd of '01 to March 15th of '09. And what the IRS has argued is that there was recoupment.

THE COURT: Yes.

MR. HIGGINS: And that there was no claim for interest. And what the -- what Grace is arguing, the reorganized debtors are arguing, quite simply is, of course there was a claim.

We don't think that recoupment describes what happened here. We think that that theory is wrong on the merits. And what happened was that there was a claim for

$6.7 million, plus interest from April 2nd of '01 through March 15th of '09, at which point because that was when the final one of the NOLs arose -- there was a number of NOLs -- net operating losses. Excuse me, Your Honor.

THE COURT: Yes. No, I know, yes.

MR. HIGGINS: Net operating losses that arose in '01, '02, each year up through '07.

THE COURT: Yes.

MR. HIGGINS: And then you had the big one for '08, which arose as of March 15th of 2009, which is why that dates critical because that's the date the return was due and the date on which the NOL came into existence, and the tax credit that result from that, which the IRS agrees to. I don't think there's any disagreement on the amount of the tax credit or anything along those lines. It's just simply now what was the interest rate in --

THE COURT: Well, that's right. And they're arguing statutory interest applies.

MR. HIGGINS: And they're arguing statutory interest. And they're arguing that, well, the post-petition claim wasn't the claim because we recouped it. But, you know, our view is, well, there was a claim. Because in order for recoupment to happen, there has to be two antecedent claims. There has to be a claim by, in this case, the reorganized debtors for the tax credit that arose

as of the -- of March 15th of '09. And, quite frankly, because of the tax credits that arose in all of the other tax years because of the respective NOLs. So that's on one side.

And on the other side, you've got the IRS's claim, Claim 18553A I think was the ultimate name it was called. And that was for the tax that arose as of March 15th of 1999 for tax year '98, the prepetition interest at the statutory rate from 3/15/99 through April 2nd of '01, plus the interest on this claim.

Now, there's a couple of reasons why recoupment really doesn't apply here. Number one --

THE COURT: Well, let me ask you this question --

MR. HIGGINS: Sure.

THE COURT: -- if I may. And I'll ask the same question of Mr. Benson from the IRS. But setoff, that's a claim. I think everyone agrees if there's setoff.

MR. HIGGINS: That's right, Your Honor. I agree with that.

THE COURT: And they say recoupment is not a claim. And in setoff, generally speaking, parties are dealing with multiple years; and in recoupment, they're dealing with one year. And isn't this a multiyear matter? I mean, we have NOLs from 2008; we have refunds for 2001 to 2011; we have a deficiency claim for 1998. Aren't all of

these things --

MR. HIGGINS: We agree, Your Honor. That's -- I just hadn't gotten there yet. But the answer to that, simply put, is yes, absolutely. You've got NOLs from '01 to '08. You know, it's funny, I've got my two very well marked up copies of Exhibits C and D, which kind of lay this out if you, you know, fix your mind to it. And, you know, I was looking at it as much from the focus on -- you know, it's amazing the amount of agreement that's here and the agreement on what the claim was and to isolate this idea behind -- the idea of what's in controversy here, which is the interest rate. So that's, I think, one major reason why equitable recoupment doesn't apply.

The other is that equitable recoupment is an affirmative defense. And so affirmative defenses, I think, insofar as the IRS says that, you know, affirmative defenses aren't claims. But we're not talking about the affirmative defense; we're talking about what the claims were before you could apply the affirmative defense. And the affirmative defense never comes into play because the IRS and the reorganized debtors agreed on what the tax amounts should be.

Now, admittedly, because of the -- I don't wish to cast aspersions, but the way in which things happen -- very often happen with the government, the refund check appears

out of the middle of nowhere in September of 2014. And discussions were then taken, well, how do we wrap this claim up, and there were discussions that were ongoing about what the interest rate was. And so, you know, the decision was taken to focus on the claim, allow the claim in that amount, and work with the IRS on the appropriate interest rate, in which ultimately led to us appearing before you today.

THE COURT: Yes.

MR. HIGGINS: I think -- so I think those are the major points that I wanted to cover, Your Honor, is that, you know, there were claims, the interest was a claim, the plan is the sole source of interest in this -- for this claim. Remember, this is a priority claim, it's an unsecured claim. So thus, absent the plan when you look at Section 1015, the definition of claim of unmatured interest, and Section 502(b)(2) and its treatment, the generic treatment for unmatured interest claims -- they're, you know, disallowed. That you come back to, sort of, the one thing, as Curly said, is it's the interest rate here and the interest rate that's set forth in the plan.

THE COURT: Do you know what the IRS interest rate was?

MR. HIGGINS: Your Honor, I believe --

THE COURT: I'll ask Mr. Benson when he appears.

MR. HIGGINS: Yeah. I think as a general matter,

it was -- during that period, it was far higher than 4.19 percent.

THE COURT: I assume that, yes.

MR. HIGGINS: And of course, you know, the financial crisis of '08. And then since then, the last 10 years really or nine years, 4.19 percent has looked to be a very attractive rate.

THE COURT: Absolutely.

MR. HIGGINS: And, Your Honor, that's really -- that's really it. This comes back to this is a claim, claims are treated under the plan, and recoupment, we never get to the issue of recoupment.

THE COURT: Okay. Thank you, Mr. Higgins. I appreciate that argument. Mr. Benson, good morning.

MR. BENSON: Good morning, Your Honor.

THE COURT: How are you?

MR. BENSON: Very well.

THE COURT: Good.

MR. BENSON: Your Honor, I'd like to first, if I may address an issue that sort of got glossed over that's in the briefing. There's much discussion of whether the interest was a claim.

THE COURT: Yes.

MR. BENSON: But in order for the plan provision that we're all talking about to apply, it's not just that we

have a claim, we must have an allowed claim. And I pointed out in my brief that because there was no final order, there was no allowed claim. There was an objection, we withdrew our claim -- our proof of claim -- debtor withdrew their objection.

THE COURT: Right.

MR. BENSON: And so as far as I'm concerned, there is no allowed claim. I would direct Your Honor to, in the definitions section, it appears in Definition 6(b). Mr. Higgins referenced an issue -- let's see -- whether something is resolved by the debtors and the claimant pursuant to Section 5.1 in the plan. I haven't read the plan since we initially -- or that section since we initially briefed it. But my recollection was that dealt with asbestos claims or some other type of claim that was not relevant to the present dispute.

So it was my reading of the plan and everything that -- all of the other sections it referred to, that we're just not dealing with an allowed claim. And so if Your Honor adopts that view, then all of these issues of is it a setoff, is this recoupment, what is this is all really irrelevant.

Moving on to the issue of setoff versus recoupment. First, I'd like to clarify another thing that I don't think was necessarily clear from the briefing. There

are really three doctrines at issue: there's what we refer to as setoff, what is traditionally referred to as setoff and that's the (indiscernible) case, which is pursuant to other common law setoff rights or Section 6402 of the Internal Revenue Code. When you have an overpayment from one year and an underpayment from another year, the IRS can net those.

THE COURT: Yes.

MR. BENSON: And that is what is always referred to as setoff. That's, you know, I'm in this Court and other Courts frequently dealing with issues of setoff. And, generally, how it comes up is you have prepetition -- the issue is are the underpayments and overpayments on the same side of the petition date or are they note, and then that gets into is 553 available.

There is what has been known as equitable recoupment, which is, as the debtors point out, is now embodied in a certain portion of the Internal Revenue Code in the 1300s, I believe. And that deals with same tax payer, usually different years, and it's the same transaction. And by transaction, you're actually talking about some kind of business transaction. And, you know, in one year -- recipient of funds in one year treats it as a gift and another year treats it as a loan being made.

And notwithstanding statute of limitations or any

other issues, the IRS can -- basically, a Court can say as a matter of consistency, we're going to -- you have to take a consistent position. And to the extent it's necessary to move money around, we'll do that. That is definitely not at issue here.

The third doctrine is sometimes known as recoupment. In the -- I'm not sure how to pronounce it -- (indiscernible) case --

THE COURT: Yes.

MR. BENSON: -- that we cite, there is much discussion of offset, but it's dealing with that doctrine. And at a certain point, I think it I cite it in a footnote, it's on Page 283, this concept that I'm getting that, which is normally known as the defense of lack of overpayment from Lewis B. Reynolds is referred -- the case is referred to as the tap root of this branch of recoupment. So I think -- and that's talking about what happened here.

And so I think part of the problem is Courts traditionally have not been entirely consistent in the use of the terms setoff, offset, and recoupment, largely because it doesn't matter in any way as much as it does in this Court because you don't have the issue of 553 versus not 553. In those contexts, everybody understands what's going on.

So what we have here is the defense of lack of

overpayment. And it goes --

THE COURT: That's not in the brief anywhere, is it, that term?

MR. BENSON: It's in my brief.

THE COURT: It is? Okay.

MR. BENSON: I believe this -- on Page 5 of my brief in the footnote, I say: The Federal Circuit used the word offset in this decision, which I believe refers to (indiscernible) -- no, Pacific Gas & Electric -- and used the word offset in its decision and referred to the relevant doctrine as defense of lack of overpayment instead of recoupment. And then I note that other Courts have used that term, that recoupment, for defense of lack of overpayment. But I do reference that in the brief; perhaps, that should have been in the body, not a footnote.

But, yeah, so what we're dealing with here is the defense of lack of overpayment, which in a bankruptcy context is the equivalent of recoupment. Because it is a defense, we're not saying we have a claim. We're just saying you say we owe you money; we believe, based on everything that happened in that tax year, we don't owe you as much. And so there is no claim to bring because, in fact, we -- they owe -- or we owe them money and that's undisputed; they don't owe us anything.

THE COURT: How do you get anything from a

bankrupt without a claim being filed?

MR. BENSON: Well, we didn't get anything.

THE COURT: Because you --

MR. BENSON: Because we said --

THE COURT: -- you did the arithmetic basically.

MR. BENSON: Yeah. And this gets to a very important point, Your Honor. You said -- asked Mr. Higgins, doesn't this involve different tax years. And the answer is in a sense, yes; but in the crucial material sense, no.

This is not overpayment versus underpayment. This is not underpayment in '98, overpayment in 2008, because an overpayment is you paid too much tax.

THE COURT: Right.

MR. BENSON: If you have a taxpayer who pays no tax and incurs numerous net operating losses, which is often the case in debtors in this Court, there can't be an overpayment because they didn't pay anything.

What's going on is effectively NOL's tax attributes that arise in 2008 are carried back and factored into the liability in 1998. So it's functionally no different than if the NOLs arose in 1998, which based on what Your Honor was suggesting, that would unquestionably be the same tax year.

When you're dealing with carry forwards/carry backs, it's the same concept. We're only talking about the

liability between the parties for 1998. It's just they're able to kick tax attributes from one year and factor them into the liability for 1998. But it is definitely note the case that we're dealing with a Bankruptcy Code 553 or a IRC Code -- IRC 6402 situation, where it's we owe them money for one year, they owe us money for another year. I would actually assume that there was no overpayment in 2008 because, generally, debtors in bankruptcy don't, except in the year of a 363 sale, generally don't have any taxable income.

I just want to address a couple more points. The debtors note that in the cases I cite, all of those involved unassessed interest. And that's not the case here; the interest was assessed. I don't think that's in any way material here because the reason all these cases deal with unassessed interest is that's the only way it comes up in refund litigation. If you have assessed interest or assessable interest, we would just suss it. There'd be no issue.

So the only way this gets litigated is you're dealing with situations where the IRS -- the statute of limitations to assess interest or whatever else has lapsed. The IRS engages -- asserts lack of overpayment based on whatever liabilities there are. The taxpayer jumps up and down and says you can't do that, statute of limitations.

And we say, no, it's recoupment, it's not offset, defense of lack of overpayment, and the Courts say that's fine. That's just because it would never come up in some other context.

But I don't think the distinction matters here. The point is we're dealing with interest that was owed initially, but then the NOLs were carried back. The NOLs are sufficient to generate a refund that exceeds the amount of the interest. And so, we have no right to payment, which would be necessary to have a claim. We unquestionably owed them money.

Finally, I think it was --

THE COURT: What was the interest rate, if you know?

MR. BENSON: It's would have -- it's based on, I forget if it's the Fed funds rate, or there's a baseline rate plus 3 percent.

THE COURT: Okay.

MR. BENSON: And so, that was much higher in 1998. Then it went to effectively zero in 2007-2007. It recently went up to 4. So I guess, you know, it fluctuated is the answer. I was not particularly focused on interest rates in 1998 when I was, I think, still in junior high, so I can't exactly -- I can't opine on that.

THE COURT: All right.

MR. BENSON: Last of all, there was a mention in

the opening brief by the debtors that effectively, they could have paid and then sought a refund. And then when they paid us the initial amount sought, it would unquestionably be 4.19 percent because they were paying us a claim under the plan, and then gotten the refund and then that would allow them to pay 4.19 percent. And so Your Honor should let them basically undo what they did and do what they say they could have done, which would have been more profitable for them.

That couldn't have happened here, I don't think, because of the deadline, basically, statute of limitations to utilize the NOL carryback. And if I'm not mistaken, the NOLs here can only be carried back 10 years. And so that would be 10 years from whenever -- or 10 years from three years from the return being due, which I believe would have lapsed in presumably March 15th or September 15th of 2012, if I'm not mistaken on that. And so --

THE COURT: Doesn't bankruptcy stay that from running?

MR. BENSON: No, Your Honor. I don't see how it would. I don't have a provision to cite for you for why it wouldn't. But from my experience, debtors always -- my understanding was that that is not the case, especially because in a sense it's not a statute. It's just an administrative rule on when you can bring things. And then

is it 106 that deals tolling, but that's only for 60 days, if I remember correctly? Sorry, Your Honor, I didn't --

THE COURT: Okay.

MR. BENSON: I wasn't prepared for that question, so I don't know. But in my experience, no one has ever argued that. And since it would be frequently advantageous for people to argue that, I'm assuming it's -- nobody has come up with an argument that would support that position.

So effectively, it couldn't have happened. They could not have done this maneuver where they would pay our claim that 4.19 percent and then get a refund because of how long it took to have the plan confirmed and go effective. And so, hypothetically, yes, that would have been a better thing for them to do; but, based on the actual facts of this case, that was not possible.

So effectively debtors made the decision, we're going to file our refund request before the plan goes effective. You know, for all anyone knew, the plan was never going to be confirmed or go effective.

And so, from our view, they did what they seemed the best at the time. And it really seems odd and sort of inequitable for them to say, based on the plan being confirmed after we did this, retroactively, the interest rate is reduced, because that is effectively the argument, I believe. It couldn't have been 4.19 percent at the time the

refund was requested because the plan hadn't gone effective. They're basically saying, based on subsequent events, the plan going effective, please undo the statutory interest rate and now apply the rate under the plan.

So I think that's all the points I came to discuss if Your Honor has any questions for me.

THE COURT: I'm still kind of -- Mr. Benson, I'm still a little bit wrapped up with the fact that we're dealing with so many different years here. In other words, when you -- the calculations in the briefs involve the NOLs, to which you add the refunds from 2001 to 2011. And you subtract the 1998 tax deficiency, and you subtract interest, and then you add over -- add in overpayment interest. So you're dealing with different years in this sort of model that the IRS is using. That's what throws me off a little bit.

MR. BENSON: Okay. And the key distinction --

THE COURT: Yes.

MR. BENSON: -- between 6402/553 offsets and what I've called recoupment, what the Courts have also called defense of lack of overpayment, is that it's crucially if -- the crucial distinction is you're not dealing with affirmative claims on both sides. It's not that they owed us for '98 and we owed them anything for 2008. It's their tax attributes that they are moving around, but there is no

overpayment on their end for any of these other tax years. And so, this is what corporate taxpayers are allowed to do; they're allowed to move things around. Individual taxpayers can do that to a more limited extent.

And if Your Honor takes a look at all the cases I cited, you know, I won't go into all of them, but you're generally dealing with attributes from different years.

THE COURT: Okay.

MR. BENSON: And that's always -- often the context where we are allowed -- you can litigate -- we, the IRS, can litigate issues that normally would be barred by statute of limitations regarding, you know, when is -- when did the tax attributes arise. We can litigate those issues, even if administratively or statutorily we couldn't independently, because we're not effectively dealing with those years. We're dealing with the year at issue for which a refund is sought. And those tax attributes are being brought into that year and are treated as now those years' tax attributes, and they're trying to use those tax attributes to lower the taxable income as they would if, you know, as anyone would do.

You know, if Your Honor makes charitable donations in a year, you take those against your income for that year. It's no different than -- well, I guess the better example would be if Your Honor sells some stock this year, doesn't

have enough taxable income to use, and you carry them forward up to 2000, I think.

But the point is, you can your capital losses for this year, bring them to the next year. They are treated for tax purposes exactly as if they arose in that year. They are, effectively, now for that year. And were we to challenge those things, that would be a recoupment issue because it's not that -- what would it be -- that you have a -- it's not an issue of overpayment versus underpayment. It's just an issue of, you've moved things around from different years and we're now litigating the year at issue.

THE COURT: But here's the thing. The refunds from 2001 to 2011, those are not a tax attribute, are they?

MR. BENSON: I'm sorry, Your Honor.

THE COURT: The refunds owed W.R. Grant for the years 2001 to 2011, which is part of this calculation, those are not tax attributes. I understand what you're saying about the NOLs, that the NOLs are tax attributes.

MR. BENSON: Yeah. I don't think that's at issue, is it? I thought the issue was '98 interest, and there was no issue about refunds. It was just about carrybacks.

THE COURT: Well, I have it in the formula that was being used that the parties added back the refunds from 2001 to 2011, and that's part of how you arrive at the ultimate number that's owed.

MR. BENSON: Is that right?

THE COURT: Or that you owe -- or that you owe, I guess.

MR. BENSON: Yeah.

MR. HIGGINS: Your Honor, I'm sorry. I'm just looking at Exhibit C, which is, you know, for us bankruptcy lawyers, it's a (indiscernible). I mean, there were a series of generated overpayments applied in '01, '02, up through '09.

THE COURT: Yes.

MR. HIGGINS: Which is when this ends. I mean, so they came from whatever that is, eight tax years if I've got it right.

THE COURT: Yes.

MR. HIGGINS: Now, your question comes back, and I -- it is, you know, what are those. And I think that that's really the fundamental part, you know, what's fundamentally at issue here. And I don't want to take away from counsel as counsel's still talking here, but I think that, you know, that that's the -- that comes down to that's the issue.

MR. BENSON: Your Honor, I thought the only issue was NOLs from '98. I know there were some refunds for other years. I thought they were relatively immaterial given the amount of money. Even if that --

THE COURT: I think the NOLs are for 1998.

MR. BENSON: The 2000 into '98, the massive NOLs.

MR. HIGGINS: It was, so there was approximately $885,000 give or take of tax credits generated '01 through '08 for a variety of reasons. I would have to go back and supply you with the detail that Grace's tax lawyers have informed me of. The '08, which is, you know, that's the --

THE COURT: Hold on one second, Mr. Higgins. Is it all right? Could it be that microphone? Let's try it again.

MR. HIGGINS: How about I come over here, Your Honor?

THE COURT: All right, okay.

MR. HIGGINS: So just operating from memory her, Your Honor. So we had 2001 to 2007, there were approximately -- and this is not in the briefing, this is what I subsequently gleaned as we were preparing for today -- is that '01 to '07 timeframe, there were a series of overpayments generated by a number of different tax attributes coming out of the those years. Whether they were NOLs or whatever they were, they generated tax credits of approximately $885,000.

The tax credit from 2008 was, of course, many, many times that size -- $9 or $10 million. I don't have the number right in front of me. And so, you know, what comes to the point here is that the IRS has taken the position

that this should be dealt with as if bankruptcy never happened, and as if the plan were never confirmed in the first place, and as if the Bankruptcy Code doesn't have specific treatments or unmatured post-petition interest and the payment of that.

So, anyway, so that's my --

THE COURT: You'll have a chance.

MR. HIGGINS: And I apologize, Your Honor.

MR. BENSON: Your Honor, so I only have the record from '98, which doesn't allow me to -- two things could have happened. Administratively, an offset, a true offset, under 6402 could have happened where, let's say, there's an overpayment in 2001 that then gets brought back and netted against the underpayment for '98. That's possible that could go into the calculation.

I vaguely recall, but I would need to check this, that some of the refunds were issued sort of out of those tax years, if that makes sense. The way the IRS does it is that you have a running account for every single tax year.

THE COURT: Yes, yes.

MR. BENSON: And, you know, I see here from the transcript, you have what they refer to as credits transferred in from various tax years. I don't know if --

THE COURT: Are you looking at Exhibit C?

MR. BENSON: No, no, no. I'm looking at something

I have myself, which I don't think I can admit. It's not properly redacted. Well, moving forward, I think given the confusion, this may necessitate further briefing. I think maybe both would be able to agree on that. And just looking at it, you know, with these complex corporate debtors, taxpayers, things go in and out all the time. So, you know, I'm looking at a 1.1 million credit that comes in and then goes out. I think this is something that would need to be determined.

If the refunds are being basically spit out of the tax years as they go along, then that's of no relevance.

THE COURT: Right.

MR. BENSON: So if, you know, it's the -- you know, again, Your Honor, you can do carrybacks from one -- or carry forwards from one year to another. If you have another refund from a third year, if that's not being fixed in the calculation, then that's just another tax year refund going out. And I don't know if the check that went out was just combining everything, or if, in fact, there are multiple checks that went out on the same day that are being included in that number.

But to the extent you're dealing with what the first scenario of -- I guess the second scenario that I described as the true setoff of overpayment for 2007, it goes back into the calculation for '98 and gigantic NOL

from, I think, it's 2008.

THE COURT: Yes.

MR. BENSON: Which looking here, I think I'm looking at is 11.5 million. There was an $11.5 million reduction in tax, which is probably just tens of millions of NOLs. That would be recoupment, and that dwarfs the other credits that are coming in. So this is going to be painful for, I guess, myself and Mr. Higgins to have to calculate this.

But I think to the extent there was a 6402 offset and that is a claim, which we dispute because there's still no allowed claim which is what matters. But to the extent there was an allowed claim that got carried back, one would need to effectively net the interest -- or one would need to calculate the interest based on the refunds that come back. And that could conceivably be 4.19 percent, and then the interest on the NOL portion would be the statutory rate.

I'm sure Mr. Higgins and I are both equally not looking forward to having to make that calculation if that's the case. Though, again, that's two contingencies: that's the refund overpayment credits were actually factored into '98, as opposed to just going out as things went along; and two, that we're dealing with a claim and particularly an allowed claim. And, again, Your Honor, I'd say if you, you know, look at the definition of allowed.

THE COURT: Yes, and you're saying it wasn't an allowed claim.

MR. BENSON: Right. It was, let's see, you know, it's allowed if there's no objection within the --

THE COURT: And there was no objection here.

MR. BENSON: And there was an objection, but then there's no objection, so that doesn't apply because there was an objection. As to which an objection to allowance was unopposed within the time provided and such objection has been overruled, which doesn't apply here. Resolved by agreement and the claimant, which is approved by final order of the Bankruptcy Court; there was no final order of the Bankruptcy Court. Resolved by agreement of the reorganized debtor and the claimant pursuant to 5.1; I don't have the full plan in front of me, but I believe when I reviewed it that did not apply.

I think it applies to certain kinds of asbestos claims. Determined by final order in the Chapter 11 cases; not applicable. And then as to which such claim is listed as an undisputed claim in Exhibit -- or listed on the undisputed claims exhibit, which has been filed pursuant to 5.1, which was not our case.

So whatever Your Honor thinks ultimately would decide on these rather nuanced tax issues, I think it's just -- it's not an allowed claim. And if it's not an allowed

claim, the interest rate in that provision does not apply, and so we don't need to get to what could be a very painful series of calculations on interest.

THE COURT: All right. All right. Thank you, Mr. Benson. Mr. Higgins.

MR. HIGGINS: Your Honor, so to go back to Section 5.1 of the plan.

THE COURT: Yes.

MR. HIGGINS: I think this is -- we got to start here, to be blunt. It says, and this at the top of Page 68: After the effective date, all objections that are filed and prosecuted by the reorganized debtors as provided herein may be (I) compromised and settled in accordance with the business judgment of the reorganized debtors without approval of the Bankruptcy Court. And that's what happened here.

THE COURT: Okay.

MR. HIGGINS: The reorganized debtors filed an objection in April of 2014. The IRS responded. There was a refund issued. And this is the point I was driving at earlier when I said that the IRS did not want to enter into a settlement agreement. The form of the settlement agreement was the withdrawal of the objection and the withdrawal of the claim. To be quite frank, Your Honor, if the reorganized debtors hadn't compromised and settled that

claim, there is no way on God's green earth that they would have withdrawn that objection. And so, that's the compromise and settlement.

There is no question that the two parties agree on the amount of the tax for 1998. There is no question that there is agreement on the amount of prepetition interest under Section 6402, I think, or whatever it is -- the section for dealing with prepetition, your normal statutory interest from the accrual date through the petition date. There is absolutely no controversy over that. That's what was compromised and settled. What is at issue here is the amount of interest that is calculate post-petition on that claim that was an allowed claim.

Now, to short circuit the government's arguments, I'm not sure that we I don't think we need to do any further briefing. In the government's opposition, it says the facts are not in dispute as stated in the response -- I'm sorry, yeah -- as stated in the response. The IRS granted a credit -- this is a tax credit -- of $11,491,000 so on and forth, attributable to the carryback of NOLs.

And as Your Honor has already observed, there were approximately $885,000 of other tax credits that were generated by other tax years. The tax credits are merely the currency with which this allowed claim were paid. Otherwise, Section 502(b)(2) and its disallowance of

unmatured interest would have no moment here. You know, I think that were we not in bankruptcy, we wouldn't have a quarrel with what counsel was saying, but we are in bankruptcy.

We are operating within the confines of a confirmed plan of reorganization that was confirmed in January of 2011. So in -- between 2011 and 2014, believe it or not, that was the length of time that that plan was -- the confirmation order was under appeal, and those appeals only terminated in late 2013, give or take, that led ultimately to Grace exiting in February of '14. So, you know, it really doesn't matter from within that construct now.

Counsel made the argument that there was two different kinds of setoff, and it's governed by Section -- for our purposes in bankruptcy by one section, Section 553. I think we all agree that doesn't apply because we got prepetition and we got post-petition, so that's off the table. Then you got equitable recoupment, which, quite frankly, we think is what the IRS is arguing.

And then they've got defense of lack of overpayment. You know, this is a line of cases that go back to Lewis D. Reynolds back in the 1920s and '30s, as I recall. And, you know, it's still -- it's, for our purposes here today, is a difference without a distinction in terms

of equitable recoupment because it's still an affirmative defense. It's an affirmative defense to a claim that was there, and so the -- that was existing as of the petition date.

And if those tax credits were generated in the post-petition years paid that claim as of March 15th of '09. Now, could Grace have written a check in March 15th of '09? Well, the answer is actually yes. Because, although Judge Fitzgerald was presiding at that point, there was a massive EPA settlement where Grace wrote a check for a quarter of a billion dollars right then and there.

And Grace could have done that, but, you know, that wasn't the time to do it because the parts -- you know, the parts hadn't stopped moving on the 10 years of the IRS looking at the 1998. Then, of course, that goes to the joint committee on taxation, a process that takes years and years and years. That was an evolution that didn't end until 2014, late 2014, when the IRS ultimately issued its refund. That claim was allowed and that claim was paid. And that claim was paid with tax credits.

That's really -- that's what I have. Thank you, Your Honor.

THE COURT: All right. Thank you.

MR. BENSON: Your Honor, if I could just take a look at taking the platform here.

THE COURT: Of course.

MR. BENSON: Your Honor, just --

THE COURT: Yes.

MR. BENSON: -- attempting to speed read this.

THE COURT: Take your time. Would you would a 5 or 10-minute break, Mr. Benson? I certainly give that to you.

MR. BENSON: Sure.

THE COURT: And you can read it quietly and a little more leisurely.

MR. BENSON: I think the immediate issue here, Your Honor, is the provision section Mr. Higgins cited is after the effected date, all objections that are filed may be compromised. And I believe this was compromised before the effective date.

MR. HIGGINS: No. Your Honor, just to recite, if I could, recite the dates. Effective date, February 3, 2014; claims fee, three other IRS claims that I mentioned at the beginning --

THE COURT: Yes.

MR. HIGGINS: They were paid approximately April 18th. The checks were cashed approximately April 23rd.

THE COURT: And those were paid on claims that were actually filed.

MR. HIGGINS: Those were paid on claims at 4.19

percent.

THE COURT: Yes.

MR. HIGGINS: So there's no argument the 4.19 percent was being paid on priority tax claims. The objection was filed on April 22nd of 2014, so approximately seven, eight weeks after the -- well, 10 weeks I guess it was -- after the effective date.

THE COURT: Okay.

MR. BENSON: Your Honor, if I could have five minutes to just take a look at this.

THE COURT: You certain -- yes, you may.

MR. BENSON: Okay.

THE COURT: Let's take a little recess and take your time reading it. I'll give you 10 minutes.

MR. BENSON: All right. Thank you, Your Honor.

THE COURT: All right? Yes, thank you.

[RECESS]

CLERK: Please rise.

THE COURT: Thank you. You may be seated. All right. Did you have anything to add, Mr. Benson, to the situation?

MR. BENSON: Two things, Your Honor. First, I mean, if you read it, the reflection of all judgments that are filed and prosecuted by the reorganized debtors may be compromised and settled. I think there's a question of

whether this was really prosecuted. Unfortunately, this is before -- well, slightly after I got to the DOJ that all this happened. So I can't, you know, testify to whether there was really a compromise versus, you know, or to agree to which we just withdrew.

More importantly, though, Your Honor, and I think this will probably require additional briefing.

THE COURT: Well, I don't think that you would -- the IRS would have withdrawn a claim if there hadn't been a compromise of that claim.

MR. BENSON: It does happen, Your Honor. Depending on how, if there's no dispute that we're not owed money, we often will just with withdraw. You know, it's not in our nature to continue to fight just to try to get some kind of settlement. So it -- I think it's a -- it happens all the time. That if someone, if there's an objection filed (indiscernible), we don't know this. It happens all the time that the IRS say do you actually agree with that and we'll say, you know, yes, and then the claim gets withdrawn.

So I don't know if that's considered a settlement. I don't really think that. If we're just told a claim should not have been filed, we withdraw. It's really only when there is a dispute about the amount of money, and we make a concession on the amount of money where we don't

necessarily agree that that's the amount, but we, for reason of litigation hazards if there's concern, that would be a settlement. There would be an exchange of documents, exchange of letters, formal settlement agreement. But, again, if it's just we have all of these NOSs which we've already carried back to withdraw your claim, we just do.

As to the more substantive issue, Your Honor, and this will require, in order for me to say confidentially I think Mr. Higgins to confidently disagree if he wants to. I think -- I'm just trying to work very rapidly on the calculator on my phone, but I think it's quite likely that most, if not all, of the abatement of tax that led to the refund was the result of the NOLs. And essentially, this -- because I'm trying to look at this very long transcript -- the handling of the abatement based upon the NOLs was roughly equivalent to the original tax recorded by the debtor.

With the views that what quite likely could have happened, it happened, is there's this $12 million liability on the books adjusted for some certain things. The debtor carries back this huge amount of NOLs sufficient to wipe out that entire liability. The actual overpayments from other years come back in, and then the refund goes out based on the overpayments.

So in terms of the interest, the refund -- the

overpayment refunds are really irrelevant. It's totally a separate thing. I mean, when you're dealing with these huge taxpayers with very complicated taxes, you get 10-year examinations because every year everything changes, and so you have things moving around by modules. And just looking here that did happen that credits came in, credits left. So I want to do the math with more time and a better calculator.

But I think it's quite possible that we have recoupment as to the original liability, and then the refund that went out was mostly attributable to those overpayments from other years. And so, when this gets calculated, the -- there's the issue -- so NOLs come back, that tax goes away, the underpayment interest gets calculated. That gets netted against the credits that have been brought in based on overpayments, and then what goes out is the difference.

So we come down to the very same -- the initial issue is who's right about 4.19 versus statutory rate. The credits just add on top of that, if that makes sense.

THE COURT: Okay.

MR. BENSON: Again, though, I'd want to be able to make the calculation a little more calmly, and I think that can be resolved with some pretty quick supplemental briefing.

THE COURT: Mr. Higgins, your position on that?

MR. HIGGINS: Well, Your Honor, I don't think we need any supplemental briefing on this. I'm going to point to the government's opposition on Page 6, the first full paragraph. It says: In this case, the IRS exercised its right of recoupment, not its right of setoff. And we've already talked about why recoupment doesn't apply here.

Note two, which is, it says: The IRS only determined the true amount that Grace's overpayment for that year, so on and so forth. And note two at the bottom of that page explains what the IRS did, or at least my understanding of what the IRS did. And I'm assuming that this is correct, is that: Specifically, the IRS granted a credit of $11,491,000 some odd dollars.

So this goes back to my original point, Your Honor. This was an allowed claim. Remember, there was an objection. There was a claim filed for $311 million; that was amended by an $11.9 million claim, okay. Comprised three elements -- tax for '98, prepetition interest, and post-petition interest at the statutory rate. Okay. Grace objected to the amount of that claim.

THE COURT: Yes.

MR. HIGGINS: Okay?

THE COURT: No question.

MR. HIGGINS: That's all that Grace did. We objected to the amount of that claim because we said that

wasn't right. The IRS responded. And then there was an agreement in that Grace then withdrew its objection.

THE COURT: Right.

MR. HIGGINS: And then a month later, the IRS withdrew its claim. And I will tell you, as I was the counsel, that was a very unusual feeling to withdraw an objection and wait around for the claim to be withdrawn.

THE COURT: I would agree.

MR. HIGGINS: And that, Your Honor --

THE COURT: Without a written agreement, is that right?

MR. HIGGINS: Yes, Your Honor. For better or for worse, without a written agreement.

THE COURT: Right.

MR. HIGGINS: And, you know, because the IRS didn't want to enter into a written agreement. That's the settlement and compromise. Otherwise, would have litigated it, you know, and we'd have gone to town on it. But it wasn't necessary because the parties agreed on what the tax was and what the prepetition interest was.

THE COURT: But that brings into play Section --

MR. HIGGINS: 5.1 of the plan.

THE COURT: -- 5.1 of the plan.

MR. HIGGINS: Top of Page 68, settlement, you know, compromise and settled, Your Honor. And that's why

we've got an allowed claim, and that's why the 4.19 percent interest -- that's the only thing we're talking about here is what's the rate of interest from April 2nd of '01 to March 15th of '09. It's 4.19 percent, and I don't think we need any further briefing for Your Honor to arrive at a decision on that point.

THE COURT: All right.

MR. HIGGINS: Thank you. Mr. Benson, yes, sir.

MR. BENSON: Looking at the footnote that Mr. Higgins just referenced.

THE COURT: Yes.

MR. BENSON: When he said granted a credit, it's better to say abatement of tax. The key is that NOLs -- and this is on Page 6 of my brief, Footnote 2 -- a credit of $11,491,201, attributable to the carryback of NOLs. So putting aside what he wanted to say a credit normally means, that was used somewhat colloquially. But the key is it's an abatement of tax based on the reduction of NOLs, plus $1.2 million for refunds for tax years 2001 through '11, which were then reduced by the remaining 5.8 million tax deficiency and $5 million in interest. So then there was the $1.9 million overpayment, and that then generates this $2 million overpayment with overpayment interest that goes into the refund.

The key, though, if I'm reading this correctly, is

that part of the refund amount was attributable to the carryback. So I think my theory was correct that the NOL comes in, it wipes out the tax liability. It wipes out the accrued interest under our theory of the amount of interest, which would be statutory rate. There's some left over, plus all the refunds; that goes out.

And so, this issue of the claim that there was offset because there were refunds is not correct. Because it just -- the order of analysis is NOLs from 2008 go to '98; that is part of the '98 year. Even though they original elsewhere, they added to that year. That is our defense of lack of overpayment. There still is an overpayment, but that's what we're making the recoupment argument that we had interest that accrued on that amount. You have these other refunds.

The check that goes out is based on the finalization of '98, based on the NOLs coming back, the interest calculation. And then all the refunds that you've accrued but haven't sent out because we've been doing this 10-year examination and you don't want to send money out and then have to ask for it to come back.

THE COURT: Right.

MR. BENSON: So I think that I remain correct that these other refunds are a totally ancillary issue. They don't go into the fundamental issue we're arguing about,

which is what interest rate applies.

THE COURT: Okay, all right. What further briefing would you give me?

MR. BENSON: It's more an issue of wanting to make sure what I just said is actually correct. I suppose that could be resolved in a quick letter within a week. I'm not talking about, you know, some massive attempt at a sort of reply. I just want to -- you know, Your Honor really focused in on this issue of the refunds.

THE COURT: That's right.

MR. BENSON: And I just want to make sure that I'm telling Your Honor the correct thing when I say that those refund -- or pardon me -- refunds for other years don't factor into the tax issue we're talking about, which is NOL carryback to '98 and then what interest -- what is the appropriate underpayment interest for that tax year. And that could be resolved very quickly.

THE COURT: All right. Well, if somebody wants to supplement their brief, I'm going to allow that.

MR. BENSON: Okay.

THE COURT: A letter to me, which you'll docket, no more than three pages. Is that sufficient?

MR. BENSON: Sure.

THE COURT: And then I'll give you a week to reply, Mr. Higgins, if you'd like.

MR. HIGGINS: Thank you, Your Honor.

THE COURT: And you can tell me that I don't need to reply, I've made my argument, and that will be fine.

MR. HIGGINS: I suspect we'll have something to say, Your Honor.

THE COURT: All right, okay. I've got a lot of numbers swimming around in my head, and I thought I had it figured out, but maybe not. So we'll see where we go on the basis of your letter. All right?

MR. BENSON: All right.

THE COURT: Anything further, folks?

MR. HIGGINS: Not from us, Your Honor.

THE COURT: All right. Well, thank you for a good argument. And with that, we'll stand in recess.

* * * * *

C E R T I F I C A T I O N

I, Sonya Ledanski Hyde, certified that the foregoing transcript is a true and accurate record of the proceedings.

Sonya Ledanski Hyde

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